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In the Supreme Court of the United States

OCTOBER TERM, 1949

No. 529

PHILLIPS PETROLEUM COMPANY, A CORPORATION, PETITIONER

v.

H. C. JONES, COLLECTOR OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and conclusions of law of the District Court (R. 29-36) are not officially reported. The opinion of the Court of Appeals (R. 39-46) is reported at 176 F. 2d 737.

JURISDICTION

The judgment of the Court of Appeals was entered on August 2, 1949. (R. 46.) A petition for rehearing was denied October 12, 1949. (R. 49-50.) The petition for a writ of certiorari was filed on January 6, 1950. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254.

QUESTION PRESENTED

Whether the Court of Appeals correctly affirmed the holding of the District Court that the execution or assignment of oil and gas leases of indefinite duration, for a valuable consideration, constitutes a sale of "lands, tenements or other realty" within the meaning of Section 3482 of the Internal Revenue Code.

STATUTES AND REGULATIONS INVOLVED

Internal Revenue Code:

SEC. 3480. IMPOSITION OF TAX.

There shall be levied, collected, and paid, for and in respect of the several bonds and other documents, instruments, matters, and things mentioned and described in sections 3481 and 3482, * * * the several taxes specified in such sections.

(26 U. S. C. 1946 ed., Sec. 3480.)

SEC. 3482 [as amended by Sec. 521 of the Revenue Act of 1941, c. 412, 55 Stat. 687]. CONVEYANCES.

Deed, instrument or writing, * * * whereby any lands, tenements, or other realty sold shall be granted, assigned, transferred, or otherwise conveyed to, or vested in, the purchaser or purchasers, or any other person or persons, by his, her, or their direction, when the consideration or value of the interest or property conveyed, exclusive of the value of any lien or encumbrance remaining thereon at the time of sale, exceeds $100 and does not

exceed $500, 55 cents; and each additional $500 or fraction thereof, 55 cents. This section shall not apply to any instrument or writing given to secure a debt.

(26 U. S. C. 1946 ed., Sec. 3482.)

Treasury Regulations 71 (1932 ed.):

Art. 84. *What constitutes real property determinable by law of State where located.*—(a) What constitutes "lands, tenements, or other realty" is determinable by the law of the State in which the property is situated. * * *

Treasury Regulations 71 (1941 ed.):

Sec. 113.81. *Definitions.*—As used hereinafter in this subpart—

(a) The term "deed" includes any instrument or writing whereby realty is assigned, transferred, conveyed to, or vested in, the purchaser or, at his direction, in any other person.

(b) The term "sold" imports transfer of title for a valuable consideration which may involve money or anything of value.

Sec. 113.84. *Conveyances Not Subject to Tax.*—In addition to the various exemptions * * *, the following are examples where the tax does not apply:

* * * * *

(i) Ordinary leases of real property for a definite term of years.

* * * * *

STATEMENT

The facts as found by the District Court (R. 29-35) are not in dispute. During the years 1942, 1943, 1944 and 1945, taxpayer purchased from landowners or acquired by assignment oil and gas leases in Oklahoma, which by their terms granted and leased exclusively unto taxpayer for a valuable consideration described land "for the purpose of investigating, exploring, prospecting, drilling and mining for and producing oil, gas and all other minerals, laying pipe lines, building tanks, power stations, telephone lines and other structures thereon to produce, save, take care of, treat, transport, and own said products, and housing its employees" for a stipulated primary term "and as long thereafter as oil, gas or other mineral is produced from said land". The leases further provided that they should terminate at the end of a year, unless operations for drilling were commenced or taxpayer paid a stipulated annual rental for the balance of the primary term. (R. 29-31.)

Taxpayer also acquired oil and gas leases in Kansas which were in all material respects the same as those purchased in Oklahoma, except that they did not cover minerals other than oil and gas. (R. 32.)

From October 26, 1920, until the stamp tax was repealed in 1926, and from 1932 until 1941, the Treasury Regulations provided that what constitutes "lands, tenements or other realty" is "determinable by the law of the State in which the

property is situated". Under the Regulations rulings were given at various times to the effect that Oklahoma and Kansas oil and gas leases were not subject to the stamp tax. However, Treasury Regulations issued in 1941 omitted any definition of the words "lands, tenements or other realty", and G. C. M. 23295, 1942-2 Cum. Bull. 271, issued in 1942, provided that "what constitutes 'lands, tenements or other realty' * * * is not controlled by the definition or scope of those terms under State law". This memorandum was given prospective force only. (R. 33-35.)

On July 14, 1945, the Commissioner assessed taxpayer with documentary stamp taxes in the amount of $9,581.55 on account of the execution and assignment of oil and gas leases. This assessment was paid September 21, 1945, and a claim for refund was filed March 1, 1946. This claim was rejected in full on June 26, 1946. (R. 32.)

On December 22, 1948, the District Court entered its judgment upholding the imposition of the documentary stamp tax (R. 36), and the court below affirmed (R. 46).

ARGUMENT

There are no conflicts and the decision of the court below is in accord with established principles of law.

1. The court below correctly held that although under state law the oil and gas leases in question might technically be labeled as "personalty", nevertheless they conveyed such substantial rights

and interests in real estate as to require the imposition of the stamp tax under Section 3482 of the Internal Revenue Code, *supra.* The Court of Appeals for the Fifth Circuit similarly decided, in *Morrow* v. *Scofield,* 116 F. 2d 17, that oil and gas leases, regardless of whether state law technically labels them as realty or personalty, are in substance transfers of an interest in realty and therefore subject to the stamp tax as conveyances of "lands, tenements or other realty" within the meaning of Section 3482. This Court denied certiorari. 313 U. S. 573.

The correctness of this approach is manifested by the fact, emphasized by the court below (R. 45-46), that in this instance state law, while affixing the label "personalty" to oil and gas leases, nevertheless treats such leases as interests in realty for many practical business purposes. See *Continental Supply Co.* v. *Marshall,* 152 F. 2d 300, 306 (C. A. 10). State law determines the nature of the interest actually created; the question then becomes whether the federal tax is applicable to such an interest, "irrespective of any particular characterization * * * in the local law." *Burnet* v. *Harmel,* 287 U. S. 103, 110; *Morgan* v. *Commissioner,* 309 U. S. 78, 80.

Moreover, since the same interest may, for technical reasons unrelated to economic realities, be labelled "personalty" in one state and "realty" in the next, it is obvious that unequal treatment of taxpayers in different states will result if the

sole test of the applicability of the federal taxing statute is the technical definition which the law of the state happens to favor. Thus, identical oil and gas leases would be subject to the federal stamp tax in Texas (cf. *Morrow* v. *Scofield, supra,* at p. 19), but not in Oklahoma (cf. *Continental Supply Co.* v. *Marshall, supra,* at pp. 305-307). Such a result would be inconsistent with the repeated holdings of this Court that taxing statutes will be applied in such a manner as to give uniform application to a nationwide scheme of taxation, unless the statute expressly or by necessary implication provides otherwise. *Burnet* v. *Harmel, supra,* at p. 110; *Morgan* v. *Commissioner, supra,* at p. 81.

2. There is no conflict with this Court's decision in *Helvering* v. *Reynolds Tobacco Co.,* 306 U. S. 110, which dealt with the *retroactive* amendment of Regulations in effect under a repeatedly reenacted section of tax statutes. Article 84 of Treasury Regulations 71 (1932 ed.), *supra,* providing that "what constitutes 'lands, tenements, or other realty' is determinable by the law of the State in which the property is situated", was *prospectively* amended by the exercise of the Commissioner's continuing rule-making power prior to the taxable years here in question (see Sections 113.81 and 113.84 of Treasury Regulations 71 (1941 ed.), *supra,* and G. C. M. 23295, 1942-2 Cum. Bull. 271 to eliminate this provision and, therefore, did not bind the court below to resort solely to state law, as contended by taxpayer, in resolving the ques-

tion of whether the oil and gas leases in question were "realty" within the meaning of Section 3482. This Court has long recognized that tax statutes and Regulations are not static and, consequently, that it is within the province of the Commissioner's continuing rule-making power prospectively to alter Regulations to conform with the dictates of experience, changing conditions and court decisions. *White* v. *Winchester Club,* 315 U. S. 32; *Helvering* v. *Wilshire Oil Co.,* 308 U. S. 90; *Morrissey* v. *Commissioner,* 296 U. S. 344. It is clear then that during the taxable years involved, the Regulations in effect prior to 1941 had no application and did not bind the court below. Moreover, even under the Regulations prior to amendment, courts were required to look to state law only for the character and nature of the instrument to be taxed under federal law (cf. *Morrow* v. *Scofield,* 116 F. 2d 17, 19), and this requirement has been met by the court below (R. 45-46).

3. Finally, there is no conflict, as asserted by taxpayer, with the decision of this Court in *Burnet* v. *Harmel,* 287 U. S. 103, where the income derived from the execution of an oil and gas lease by way of an initial bonus and royalties from the subsequent production of oil and gas was held to be ordinary income and not income from the sale of a capital asset. Taxpayer argues therefrom that the execution of an oil and gas lease cannot be considered a sale for purposes of imposing the stamp tax. But this Court, since its decision in

the *Harmel* case, has held that the assignment of an oil and gas lease for a valuable consideration is a sale (*Anderson* v. *Helvering,* 310 U. S. 404), and taxpayer necessarily has no argument with this proposition (Pet. 8). It contends, however, that a different rule must obtain upon the original execution of a lease. There is no merit or foundation to this putative distinction, for whether the lease be executed or assigned, the same bundle of rights and interests in realty is transferred and for a valuable consideration. Both constitute a sale of an interest in realty within the meaning of Section 3482.

CONCLUSION

There are no conflicts with the decisions of this Court or other Courts of Appeals, and the decision of the court below is in accord with established principles of law. No reviewable issue is presented and it is, therefore, respectfully submitted that the petition should be denied.

Respectfully submitted,

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